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CENTRAL INTELLIGENCE AGENCY
Directorate of Intelligence
8 November 1963

CURRENT INTELLIGENCE MEMORANDUM

SUBJECT: Comments on Ex-Chancellor Adenauer's Views Regarding Western Exploitation of Soviet Economic Difficulties*

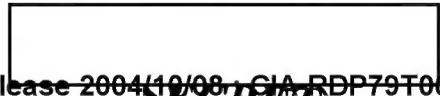
SUMMARY

We agree with the broad sweep of ex-Chancellor Adenauer's view of the problems facing the Soviet economy, although he paints the picture in somewhat darker tones than we would. We do not believe that the Soviet economy is in as dire shape as Adenauer implies in saying that it is in one of its "biggest crises" since the October Revolution. His analysis of the favorable effect that the extension of additional Western credit would have on the Soviet economy is correct. On the other hand, we believe that Adenauer greatly exaggerates the political leverage which the present Soviet economic situation provides for Western exploitation.

1. Adenauer's judgment that the Soviet economy is currently facing serious difficulties relative to its objectives is, we believe, correct. Even before the bad harvest of 1963, the USSR was straining under the burden of simultaneously pursuing three objectives: (1) the arms and space races; (2) rapid industrial growth; and (3) raising the standard of living of the Soviet population.

2. For the last few years, agriculture has stagnated and the rate of growth of industry has

*This memorandum has been prepared jointly by OCI, ONE, and ORR.



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slowed down. The volume of housing construction leveled off in 1959 and has declined since then. Industrial investment which formerly increased 10 percent or more annually has grown at 4 or 5 percent per year since 1960. The construction industry has experienced considerable difficulties in completing projects, especially in the chemicals industry.

3. The bad 1963 harvest has convinced the Soviet leadership that a massive build-up of fertilizer capacity is required to assure growing food supplies for the Soviet bloc. The goal for 1965 is 35 million tons of fertilizer, compared with 20 million tons in 1963. The tentative goal for 1970 seems to be 100 million tons. The Soviet Union cannot approach this long-run goal without substantial imports of equipment from the West. Adenauer's description of the difficulties experienced by the Soviets in producing fertilizer equipment and in building fertilizer plants is, we believe, essentially correct.

4. There is no question of the importance to the Soviet economy of additional Western credit. The Soviet hard currency payments deficit has averaged about \$300 million a year from 1960 through 1962 and will undoubtedly be higher in 1963. Repayment of past medium-term credit in 1963 almost equals the new credit extended by Western suppliers. The alternative possibility of using gold reserves is rapidly dwindling. Following payment for the Western grain already purchased (excluding possible purchases from US), the Soviet gold reserves will in 1964 probably fall to about \$1.5 billion. This reserve is approaching a minimum level that must be held against possible future harvest failures. Thus, in the absence of longer term credits from the West, the USSR is faced with the possibility of reducing imports at a time when it badly needs to increase them.

5. We judge that the Soviet economy (aided only by the European satellites) cannot carry through the fertilizer development program (not to mention synthetic fibers and plastics) without significantly

curtailing the arms and space build-up or further slowing rates of growth of other sectors of industry. In view of these conditions, additional Western credits will contribute to maintenance of Soviet arms expenditures or to general industrial growth. In the absence of additional Western credits, an accelerated fertilizer program would be at the expense of other programs.

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a restriction of NATO machinery exports below current levels either directly or by a reduction of credit--would penalize Soviet economic growth even more. Under these conditions, the Soviet leaders would have to retrench still further--reduce arms expenditures somewhat, or accept for the time being an even lower rate of growth.

7. We believe that Adenauer somewhat understates Soviet capabilities to get along in the face of reduced Western exports. In the first place, the problem of grain supply which has arisen in 1963 is largely the result of abnormally bad weather. The return of normal weather conditions probably would restore food supplies per capita to tolerable though not record (1958 and 1961) levels. However, in the long run the agricultural problem could become even more pressing and harder to solve. The problem stems from the desire of the people and the leaders for a significantly improved diet at the same time that land productivity in the New Lands is falling. Soil erosion in the New Lands resulting from poor agriculture practices cannot be rectified without a sharp cutback in land under cultivation.

8. Second, Adenauer may exaggerate the significance of present Soviet imports from the West. The USSR itself produces by far the largest part of its requirements for machinery and equipment, and about two thirds of Soviet imports of machinery and equipment come from the European satellites. The importance of the imports from the West lies in the high quality and the advanced technology which is embodied in Western equipment. The dependence of the USSR on the West for chemical equipment is greater than for

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other types of equipment. Even so, the denial of equipment from NATO countries (which might not be joined by all other Western countries) would not prevent the USSR from increasing fertilizer capacity. It would, however, mean that the construction program would be significantly slower and more expensive and that reductions in other industrial or military programs would be correspondingly larger.

9. Thirdly, we do not concur in Adenauer's assessment of the urgency of the large-scale industrialization of Eastern Siberia. We have no evidence that the Soviets are planning any significant increase in the present moderate but steady program of development of Eastern Siberia. Nor do we see that such a development is called for by the dispute with China. The USSR may have to increase its military defenses along the Chinese border at some time in the future, but an uneconomic industrialization of this vast area would not contribute much to the defense.

10. We also disagree with some of Adenauer's detailed facts. However, these differences do not undermine the general validity of his analysis, but make the Soviet problems sound somewhat grimmer than we think they are. For example, we do not believe there is a general electric-power shortage which is limiting industry. Household consumers and farms are severely limited in electric-power supplies, but we have evidence of only occasional spot shortages in industry. Secondly, Adenauer cites a 50-percent fulfillment of planned chemical investment in 1962. Chemical investment in 1962 was actually underfulfilled by only 10 percent. Finally, the 30-percent price increase in 1962 did not apply to all agricultural products as Adenauer implies, but only to meat and butter.

11. In our view, Adenauer greatly exaggerates the political leverage which the Soviet economic situation provides for Western exploitation. We question the validity of his central thesis--if the USSR is denied access to Western markets and credits, the resulting economic crisis in the Soviet Union

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might be so serious that the West "might obtain genuine political concessions, as otherwise the Soviet Union might not be able to hold out in the face of the Chinese-Soviet conflict." Although Adenauer makes no specific reference to the questions of Berlin and German reunification, it is clear that he has these matters in mind when he predicts that the Soviet leaders, in order to insure their access to Western markets for vitally needed equipment, "would be prepared to change their policies vis-a-vis the West."

12. If this is in fact what Adenauer has in mind, he appears to be underrating the fundamental position of Berlin and Germany in Soviet policy. The definitive recognition of the permanence and legitimacy of the status quo in Eastern Europe, including the partition of Germany, has for long been the main concern of the USSR's policy toward the West. Even though the proposed measures might place serious strains on the Soviet economy, it is highly unlikely that these measures alone would cause the USSR to accept Western terms for German reunification.

13. We believe, moreover, that the Soviet reaction to the measures Adenauer advocates would be almost the exact opposite of the "genuine political concessions" he forecasts. The Russians almost certainly would immediately interpret such measures as the forerunner of a grave Western challenge carrying a strong probability of developing into a dangerous military confrontation. Their outlook has long been conditioned by an almost pathological suspicion and fear of resurgent German military power. Throughout the post World War II period, the Soviet leaders have tended to exaggerate every step in Western policy toward the Federal Republic as being aimed at developing a formidable position from which the West Germans could use force to bring down the East German regime and subsequently the entire Soviet empire in Eastern Europe. This preoccupation with growing West German strength is the force that has motivated Moscow's diplomatic offensive over the past five years to consolidate the East German regime and the present Soviet bloc frontiers in Central Europe before West

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Germany reaches a "position of strength" which could confront the USSR with a serious challenge. As Khrushchev told Walter Lippmann in April 1961, there must be a German settlement before "Hitler's generals with their twelve NATO divisions" acquire nuclear weapons from France and the US. Before this happens, he said, there must be a peace treaty defining the frontiers of Poland and Czechoslovakia and stabilizing the existence of East Germany. Khrushchev contended that in the absence of such a settlement, West Germany some day will drag NATO into a war for the unification of the country and restoration of the old eastern frontiers.

14. In addition to ruling out any possibility that Western economic pressures in themselves could compel Moscow to abandon its "two Germanys" policy, we would also question Adenauer's emphasis on the Sino-Soviet contest as a determining factor in bringing the USSR to grant major political concessions as the price of escaping a Western economic boycott. For the foreseeable future, Peiping's challenge to Moscow will continue to be primarily a political competition for influence and control in the international Communist movement, not a military threat requiring far-reaching revisions in Soviet policy toward the West.